Scotiabank.

GLOBAL ECONOMICS & FX STRATEGY

FOREIGN EXCHANGE OUTLOOK

September 25, 2025

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Market Tone

Back in the summer, we had expected the rapid sell-off in the US dollar (USD) to extend further. Instead, currency markets tended to consolidate through mid-year, allowing the USD to stabilize. Some relaxation in trade tensions (after the US reached a trade deal with the European Union, for example) allowed an oversold USD to strengthen in July and gains extended through to early August until the release of a surprisingly poor US labour market report checked its rise and effectively—it now seems—mark the high point of the USD recovery. Despite the stabilization in the USD through mid-year, we remain bearish on its outlook and maintain forecasts anticipating moderate losses over the balance of this year and more weakness through 2026 amid a litany of challenges facing the currency and the US economy.

The surprisingly weak July Non-Farm Payroll data triggered a sharp fall in US yields and prompted markets to revise the outlook for the Fed policy rate, weighing on USD sentiment. More weak labour market data (and significant downward revisions to prior reports) alerted investors to the risk of more aggressive rate cuts over the balance of this year and into 2026. Pressure from the US administration for lower interest rates has also weighed on USD sentiment and the White House's manoeuvring around the make-up of

Continued on next page …

FX Forecasts

		2024a	2025f	2026f	2025f Q1a	Q2a	Q3	Q4	2026f Q1	Q2	Q3	Q4
Major Currencies												
Japan	USDJPY	157	135	125	150	144	140	135	132	132	125	125
Euro zone	EURUSD	1.04	1.16	1.22	1.08	1.18	1.16	1.16	1.18	1.18	1.22	1.22
	EURJPY	163	157	153	162	170	162	157	156	156	153	153
UK	GBPUSD	1.25	1.40	1.48	1.29	1.37	1.40	1.40	1.43	1.43	1.48	1.48
	EURGBP	0.83	0.83	0.82	0.84	0.86	0.83	0.83	0.83	0.83	0.82	0.82
Switzerland	USDCHF	0.91	0.79	0.76	0.88	0.79	0.79	0.79	0.78	0.78	0.76	0.76
	EURCHF	0.94	0.92	0.93	0.96	0.93	0.92	0.92	0.92	0.92	0.93	0.93
Americas												
Canada	USDCAD	1.44	1.34	1.28	1.44	1.36	1.36	1.34	1.32	1.32	1.28	1.28
	CADUSD	0.70	0.75	0.78	0.70	0.73	0.74	0.75	0.76	0.76	0.78	0.78
Mexico	USDMXN	20.83	19.26	20.06	20.47	18.75	19.07	19.26	19.45	19.64	19.84	20.06
	CADMXN	14.48	14.37	15.67	14.23	13.78	14.02	14.37	14.73	14.88	15.50	15.67
Brazil	USDBRL	6.18	5.52	5.62	5.71	5.43	5.44	5.52	5.55	5.58	5.62	5.62
Chile	USDCLP	995	890	870	951	932	910	890	880	870	870	870
Colombia	USDCOP	4,406	4,149	4,143	4,183	4,100	4,081	4,149	4,175	4,156	4,162	4,143
Peru	USDPEN	3.74	3.56	3.60	3.68	3.54	3.49	3.56	3.64	3.61	3.60	3.60
Asia-Pacific												
Australia	AUDUSD	0.62	0.66	0.70	0.62	0.66	0.64	0.66	0.68	0.68	0.70	0.70
New Zealand	NZDUSD	0.56	0.62	0.64	0.57	0.61	0.60	0.62	0.62	0.62	0.64	0.64

f: forecast a: actual

CAD FX Forecasts

Canadian Dollar Cross-Currency Trends

FX Rate	Spot 25-Sep	25Q1a	25Q2a	25Q3f	25Q4f	26Q1f	26Q2f	26Q3f	26Q4f
AUDCAD	0.91	0.90	0.90	0.87	0.88	0.90	0.90	0.90	0.90
CADJPY	107	104	106	103	101	100	100	98	98
EURCAD	1.63	1.56	1.60	1.58	1.55	1.56	1.56	1.56	1.56
USDCAD	1.39	1.44	1.36	1.36	1.34	1.32	1.32	1.28	1.28

Market Tone

the FOMC has only added to market worries about the potential infringement on Fed policy independence that changes to the policy-making body might imply.

Scotia recently revised its outlook for the Fed to include more easing this year and a drop in the Fed funds target to 3.00% next year. The White House thinks the policy rate should be much lower. While the Fed policy easing cycle appears likely to extend further in 2026, other core major central banks look increasingly poised to move to neutral or, in the case of the Bank of Japan (BoJ), tighten interest rates modestly. Interest rate spreads have moved against the USD over the past few weeks but are likely to compress further, undercutting the attractiveness of the USD. We also expect trade policy to contribute to heightened uncertainty and slower US economic momentum this year and next, meaning growth differentials between the US and Europe as well as Asia should also narrow. Reduced growth and yield advantages will erode the notion of “US exceptionalism” that helped launch and sustain the USD on its elongated bull run following the 2007/2008 US financial crisis.

In addition to the prospect of a significantly lower policy rate, we expect weak fiscal policy settings to weigh on the USD outlook. Following the passage of President Trump’s recent tax bill, work done by our Scotia Economics colleagues suggests that the wider US fiscal deficit alone (which may reach close to 7%/GDP over the next few years under our base case assumption) likely means a 2.6–3.6% drop in the broad value of the USD through 2026 and more losses in the medium term.

A weak phase in the USD, driven at least in part by weak fiscal policy would be very much in keeping with the broad, historic evolution in the US exchange rate since the 1970s. Bouts of USD strength are typically driven by superior fundamentals and yields on US assets while bearish USD phases have typically reflected rising investor concerns about structural negatives that have developed in the US economy, reflected by large and persistent trade and fiscal shortfalls (as was the case in the 1980s and again in the early 2000s when the US “twin deficits” drove the USD sharply lower).

A final point to consider in the broad outlook for the USD is the abiding impression that a weaker exchange rate may be part of the aggressively mercantilist policy the US administration is pursuing. While the desire for a lower USD has not been explicitly stated, US officials have not protested the 11% or so decline in the USD versus the core majors since the start of the year, suggesting the tacit endorsement at least of its decline.

To some extent, the sharp fall in the USD this year suggests that a lot of the negative factors around the USD are already at least partially priced in. This may mean that the USD holds in a lower range over the course of the next few months until markets get a stronger sense of how much easing the Fed is likely to undertake—and how quickly those rate cuts are likely to emerge—as well as the extent to which tariff policy will dampen US growth.

We think there are several market-driven pointers that suggest the balance of risks remains tilted firmly towards a weaker USD emerging in the medium to longer term. Options pricing continues to reflect a mild premium for dollar puts over calls for 3m tenors. Longer-term pricing reflects a greater implied probability of the USD trading lower against the euro (EUR) into the end of this year and next. Record gold prices are another pointer in support of the weak dollar narrative. Finally, we note that the evolution in broader dollar price action continues to track quite closely the pattern of trade in the exchange rate in late 2016 and through 2017, around the election and early stages of President Trump’s first term, in other words. If that pattern remains any sort of guide, the USD may steady or firm modestly in the next few months before sliding to new cycle lows in H1 next year.

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Federal Reserve and Bank of Canada Monetary Policy Outlook

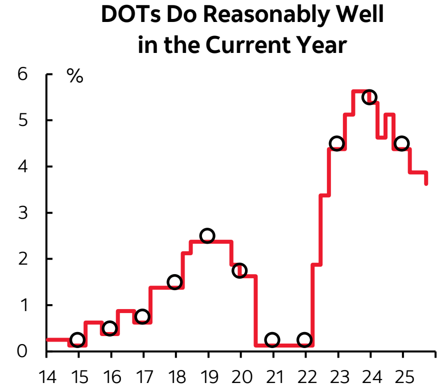
FEDERAL RESERVE—HIGH STAKES

We forecast a series of 25bp cuts that take the fed funds rate down to 3% by 2026Q2. We're conflicted on the reasons and there is significant uncertainty including about how it ultimately plays out.

The median FOMC projection is for a total of 75bps of cuts this year including September's, followed by cutting down to 3½% by some time next year. The dots are highly dispersed in both years. The in-year dots usually perform very well when we get to this time of year versus the later guesswork. The signal is that more easing is necessary to achieve what is essentially the same macro projections as previously.

The rationale offered by Chair Powell et al is that they are now more concerned about the full employment side of the dual mandate than the price stability mandate. Annual nonfarm revisions and the weak pattern of payroll changes since then have motivated a bias to take out insurance against any further erosion of the labour market. This is paired to Powell's view that tariffs are likely to add to coming inflationary pressures but only in transitory fashion that he is prepared to look through. Powell's claim that they are not on a pre-committed path seems to be inconsistent with this bias.

Chart 1



Sources: Scotiabank Economics, Bloomberg.

One reason we are conflicted is that the labour market is still tight in an economy that remains in excess demand marked by a positive output gap. Job growth has slowed but so has the supply side as immigration policy has sharply curbed growth in the labour force. Chair Powell's concern about the job market is inconsistent with his estimate of the monthly nonfarm breakeven rate in the 0–50k range which is what we've been getting.

Second, it's unclear that upside risks to inflation may be transitory. The Fed has seriously misjudged this in the past. Tariffs are only one subset of long wave developments in global supply chains that are grappling with myriad forms of more intense border risk and how to adapt. A lot of spare capacity may have to emerge to downplay concerns that consumer prices and hedonic adjustments may well suffer in the aftermath for a potentially long period.

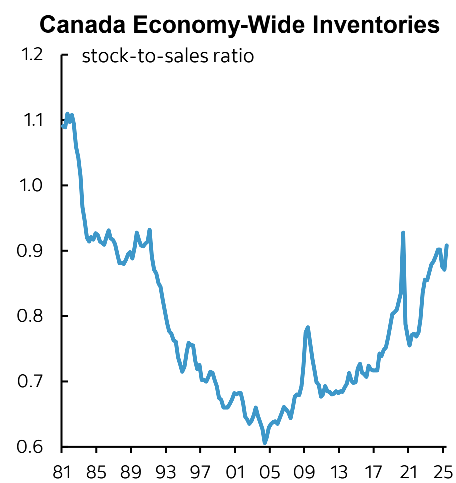
BANK OF CANADA—FINETUNING

The BoC is already within a neutral range and at the fine-tuning stage of adjustments. Our forecast is for one more rate cut but with uncertain timing. The October decision will be informed by data, but an argument to skip could be based on waiting for the Federal budget on November 4th.

Scotia Economics successfully leaned against speculation toward further rate cuts ever since March. Our call changed when the facts changed in ways no one anticipated. The BoC was likely to be more concerned about the US economy given a suddenly weaker job market including large revisions. Canada ended many retaliatory tariffs against the US. Canada lost over 100k jobs in the past two months. Various measures of core inflation including revisions have suddenly subsided. The Federal budget has been delayed again. GDP surprised weaker in Q2 with soft tracking in Q3.

Nevertheless, the case for greater BoC easing is soft. There is limited spare capacity. Fiscal policy is likely to add stimulus. Global supply chain developments add to longer-run inflation risk. Inventory padding, wage settlements and terrible worker productivity are signs of cost pressures in domestic supply chains. A path to a better outlook could include reasonably successful trade negotiations, fiscal supports, continued gains in interest-sensitive spending, lagging effects of an earlier immigration surge on the economy, and the shock-absorbing role of a flexible exchange rate.

Chart 2



Source: Scotiabank Economics, Statistics Canada.

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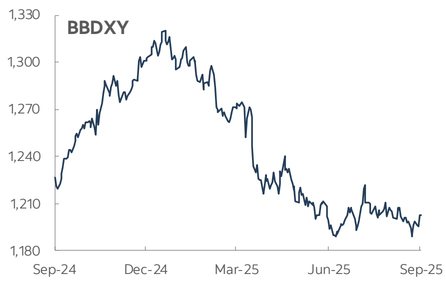
North America

USD

Expecting renewed USD weakness on Fed cuts and longer-term cyclical risks **Current spot 1208.55**



Source: Bloomberg.

USD—The USD has spent much of Q3 bound within a flat range, with congestion centered around 1200 (BBDXY). The bear trend that characterized much of its YTD decline looks to have flattened out, despite a fresh marginal low broken in mid-September around the FOMC's latest 25bps rate cut. Our bearish USD forecast is fundamentally driven by an outlook for relative central bank policy that anticipates considerable easing from the Fed, delivering an erosion of the support offered by wide interest rate differentials. Longer-term cyclical considerations are an added bearish driver, as wide fiscal and current account deficits are expected to weigh on the USD.

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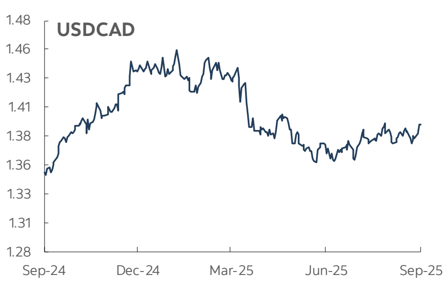
USDCAD

Bullish CAD outlook remains underpinned by relative central bank policy **Current spot 1.3943**



Source: Bloomberg.

USDCAD—The CAD's recent performance has been challenged by shifting fundamentals and a renewed dovishness from the Bank of Canada (BoC). Our outlook remains constructive, as we still anticipate less easing from the BoC relative to the Fed and thus look to support from interest rate differentials. In terms of price action, USDCAD's Q3 chart reveals range-bound movement. Longer-term charts suggest considerable resistance around 1.40, and we would expect the level to limit any upside. Our bearish USDCAD (bullish CAD) view remains intact, and we hold a Q4 2025 target of 1.34.

Scotia Forecasts	Q3-25	1.36	Q4-25	1.34	Q1-26	1.32	Q2-26	1.32

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USDMXN

MXN—Expected to weaken amid long-term challenges **Current spot 18.50**

Source: Bloomberg.

USDMXN—The Mexican peso (MXN) faces long-term challenges due to weak private sector investment, limited fiscal space for countercyclical policies and uncertainty around USMCA renegotiations. While USD weakness has temporarily supported the MXN, strength may be short-lived. Banxico is expected to continue easing alongside the Federal Reserve, with a terminal rate of 7.00% anticipated year-end. Therefore, a decline in the carry-to-volatility Sharpe ratio could reduce the attractiveness of peso-denominated assets, increasing downside risks for the currency. Consistent with the decline in the peso's volatility adjusted carry, it has fallen out of the top tier of global FX performers. We forecast USDMXN at 19.26 by the end of the year.

Scotia Forecasts	Q3-25	19.07	Q4-25	19.26	Q1-26	19.45	Q2-26	19.64

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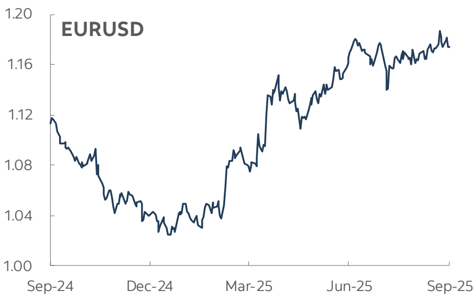
Major Currencies

EURUSD

ECB's neutral shift delivers fresh multi-year highs in EUR; remain bullish **Current spot 1.1656**



Source: Bloomberg.

EURUSD—Conviction in our bullish EUR outlook has been strengthened by recent developments. The European Central Bank's (ECB) latest policy meeting underscored a decidedly neutral bias and a preference for maintaining current policy settings. We see scope for fundamentally-driven EUR gains in an environment of renewed Fed easing and look to added upside as the market removes its pricing of ECB cuts. The EUR's Q3 performance was marked by renewed strength and a push to a fresh multi-year high above 1.19. We remain longer-term bulls, seeing upside risk to our Q4 2025 target of 1.16 as we look to continued gains through 2026 with a Q4 forecast of 1.22.

Scotia Forecasts	Q3-25	1.16	Q4-25	1.16	Q1-26	1.18	Q2-26	1.18

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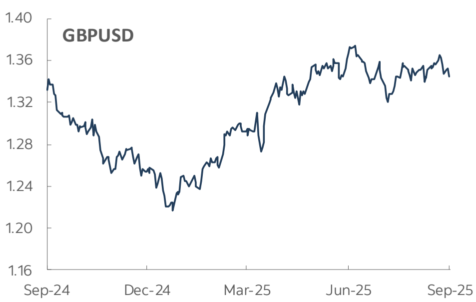
GBPUSD

GBP fundamentals remain solid on BoE/Fed outlook, with added boost from easing fiscal concerns **Current spot 1.3335**



Source: Bloomberg.

GBPUSD—The GBP's YTD rally stalled in Q3, as the pound moved into a flat range with wide congestion around 1.35. The pound's fundamental outlook remains bullish given the BoE's cautiously neutral stance and a forecast that anticipates relatively less easing than the Fed. Interest rate differentials have pushed to fresh highs, reaching levels seen in mid-2023, offering the GBP a critical source of fundamental support. Political uncertainty relating to the UK's fiscal outlook has moderated considerably, shifting sentiment in a constructive manner. We are bullish GBP targeting 1.40 by Q4 2025 and 1.48 by Q4 2026.

Scotia Forecasts	Q3-25	1.40	Q4-25	1.40	Q1-26	1.43	Q2-26	1.43

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USDCHF

CHF's sentiment-driven gains outweigh SNB's return to zero lower bound **Current spot 0.8002**

Source: Bloomberg.

USDCHF—The Swiss franc remains one of the best-performing currencies YTD with a 14% gain vs. the USD. The franc continues to trade well above levels implied by fundamentals, owing to safe-haven flows driven by broader concerns related to trade policy uncertainty and geopolitical tensions. Global investors have also favoured the franc relative to other traditional havens like the JPY and USD, magnifying sentiment-driven gains. The SNB has sought to push back on CHF strength by reducing its policy rate to the zero lower bound, and is openly discussing the renewed use of unconventional policy easing. Our forecast anticipates an extension of EURCHF's recent consolidation around its recent multi-year lows.

Scotia Forecasts	Q3-25	0.79	Q4-25	0.79	Q1-26	0.78	Q2-26	0.78

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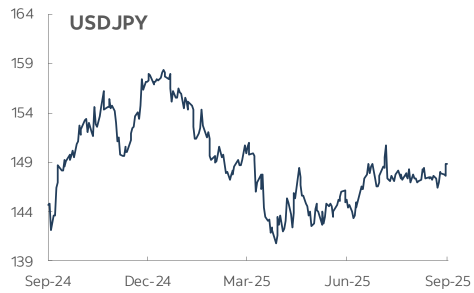
Major Currencies *(continued…)*

USDJPY

JPY set for renewed strength as BoJ looks to deliver hike before year-end **Current spot 149.76**



Source: Bloomberg.

USDJPY—The yen's fundamentals are improving as market participants look to the possibility of renewed tightening at the BoJ. Policymakers have indicated a desire to raise rates before the end of the year, aiming for a 25bps hike in either October or December, and yield spreads have narrowed considerably. The central bank has also sought to push back on any concerns about the possibility of an extended pause, given political uncertainty related to the LDP leadership race that will be held on October 4th. We look for a bearish break of the recent USDJPY range, targeting 135 by Q4 2025 and 125 by Q4 2026.

Scotia Forecasts	Q3-25	140	Q4-25	135	Q1-26	132	Q2-26	132

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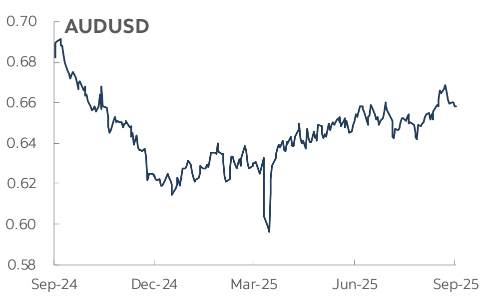
Australia

AUDUSD

AUD recovery set to extend as markets reassess RBA rate path **Current spot 0.6529**



Source: Bloomberg.

AUDUSD—We are bullish AUD as it remains well supported in an environment of easing trade tensions and softened China-related growth concerns. Australia's terms of trade are seeing a renewed improvement and interest rate differentials are pushing higher as market participants moderate their expectations for lower rates from the RBA. Recent inflation data have surprised to the upside, forcing markets to price a slower pace of easing and consider the possibility of an early end to the RBA's easing cycle. Our bullish AUD forecast targets 0.66 by Q4 2025 and 0.70 by Q4 2026.

Scotia Forecasts	Q3-25	0.64	Q4-25	0.66	Q1-26	0.68	Q2-26	0.68

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Latin America

USDBRL

BRL—Supported by yields and carry interest **Current spot 5.3542**

Source: Bloomberg.

USDBRL—BRL has had a very strong year in 2025, gaining over 15% relative to the greenback (5th best among the 32 most liquid FX). Behind the strong showing are 3 important factors: a) almost 300bps of hikes by the BCB, b) a sharp improvement in the real's carry-vol ratio (4th best carry-vol Sharpe ratio among the 32 most liquid FX), and c) rising optimism that following next year's election in October, we could see some improvements in the fiscal story (we think it's still too soon to speculate on this front).

Scotia Forecasts	Q3-25	5.44	Q4-25	5.52	Q1-26	5.55	Q2-26	5.58

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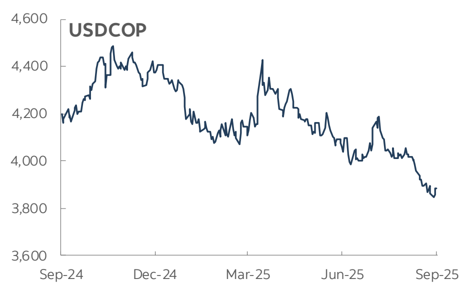
USDCOP

COP—Tight domestic policy drives carry demand **Current spot 3,902.00**



Source: Bloomberg.

USDCOP—The COP is trading at its strongest since May 2024. Some structural forces are behind the movement, namely the international backdrop appears less restrictive than expected at the beginning of the year now that the Federal Reserve has resumed its easing cycle. On the home front, strong domestic demand and sticky inflation are supporting the contractionary stance of the central bank for longer than expected, sustaining the COP's attractiveness for carry trade operations. However, current levels are well below our fundamental value calculation, something that we attribute due to expectations surrounding the financing operations of the Government in international markets and uncertainty about how long that will continue.

Scotia Forecasts	Q3-25	4081	Q4-25	4149	Q1-26	4175	Q2-26	4156

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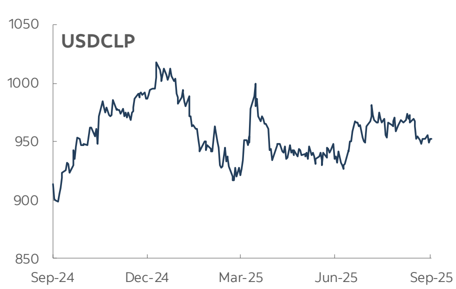
USDCLP

CLP—Held back by focus on election **Current spot 960.20**



Source: Bloomberg.

USDCLP—The CLP has remained broadly stable near CLP950 versus the USD, despite a slightly firmer USD generally and a 2.8% increase in copper prices. Political uncertainty ahead of the November 16th presidential election continues to weigh on the peso, while most Latam currencies have appreciated. The central bank's daily USD purchases (up to USD25mn) and weekly dollar sales by the MoF (up to USD300mn) have had a neutral net impact. The Fed's first rate cut on September 17th and stronger copper fundamentals support our view of CLP appreciation toward 890 by year-end. A potential market-friendly runoff outcome in December and recent signs of political moderation reinforce this scenario. We expect the CLP to benefit from improved external conditions and reduced domestic risk premiums.

Scotia Forecasts	Q3-25	910	Q4-25	890	Q1-26	880	Q2-26	870

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Latin America *(continued…)*

USDPEN

PEN—Stability bolstered by firm metals, softer USD **Current spot 3.5015**

Source: Bloomberg.

USDPEN—The PEN remains one of the most stable currencies in the region. As of the end of August 2025, it reached its strongest level in nearly five years—since September 2020—trading at 3.53 per US dollar. Despite the zero interest rate differential between the Federal Reserve (FED) and the Central Reserve Bank of Peru (BCRP), the sol has remained strong, driven by a weakness in the US dollar index (DXY) and elevated metal prices, particularly copper and gold. In the short term, we expect the sol to remain around 3.50 per dollar, and by year-end, we project it will trade around 3.56 per dollar, amid the uncertainty that could arise toward the end of the year due to the upcoming 2026 presidential elections.

Scotia Forecasts	Q3-25	3.49	Q4-25	3.56	Q1-26	3.64	Q2-26	3.61

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